STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

Illinois Bell Telephone Company	:	
	:	
Filing to increase Unbundled Loop and Nonrecurring Rates	:	**ICC Docket No. 02-0864**
	:	

STAFF OF THE ILLINOIS COMMERCE COMMISSION'S

SUMMARY OF POSITION

NOW COMES the Staff of the Illinois Commerce Commission, by and through its attorneys, and, for its Summary of Position, states as follows:

I. Introduction

The Staff submits this Summary of Position pursuant to direction of the Administrative Law Judge. This pleading is not one contemplated by the Public Utilities Act, 220 ILCS 5/1-101, et seq., or the Rules of Practice before the Illinois Commerce Commission. See, generally, 83 Ill. Admin. Code 200.10, et seq. The Staff's position in this proceeding is fully set forth in its extensive testimony and its Initial and Reply Briefs. To the extent that any matter raised by the Staff either in its testimony, its Initial or Reply Briefs, or other pleadings filed in this proceeding, this does not constitute a waiver of such matter, nor should it be so construed.

In this proceeding, the Staff states that it has carefully analyzed SBC's proposed unbundled network element loop (UNE-L) rates and nonrecurring charges, along with accompanying cost studies, testimony, and associated information. Based upon its review, the Staff recommends that the Commission not adopt SBC's proposal as filed. Instead, Staff has proposed both recurring rates and non-recurring charges, and urges the Commission to adopt these rates and charges.

II. General Issues

A. Legal Requirements for Setting Rates

1. TELRIC Pricing Principles

a)

Section 251(d) of the Telecommunications Act of 1996, which establishes the basic standards for UNE prices requires that UNE rates be, inter alia, cost based, determined without reference to a rate of return proceeding. Staff IB at 16 et seq, citing 47 U.S.C. §251(d)(3). The FCC, which the Congress directed to make rules implementing this section, adopted rules requiring the use of total element long-run incremental cost ("TELRIC") principles in determining UNE rates. Staff IB at 16, et seq.; see also 47 C.F.R. §51.505, *First Report and Order*, In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Interconnection between Local Exchange Carriers and Commercial Mobile Radio Service Providers, CC Docket Nos. 96-98 and 95-185, FCC 96-325, 11 FCC Rcd 15499; 1996 FCC LEXIS 4312; 4 Comm. Reg. (P & F) (August 8, 1996 Released; Adopted August 1, 1996) (hereafter, "*First Report and Order*" or "*Local Competition Order*"). In promulgating its TELRIC rules, the FCC rejected the use of embedded costs in calculating UNE rates, and required that costs be:

> [T]he forward-looking economic cost for interconnection and unbundled elements would be based on **the most efficient network architecture**, **sizing, technology, and operating decisions that are operationally feasible and currently available to the industry**. **Prices based on the least cost, most efficient network design** and technology replicate conditions in a highly competitive marketplace by not basing prices on existing network design and investments unless they represent the least cost systems available for purchase.
>
> Id., ¶683 (Emphasis added)

The FCC permitted one departure from this regime, that being the decision to base costs on existing ILEC wire centers. Id., ¶685. The U.S. Supreme Court has found the TELRIC rules to be entirely consistent with the pricing provisions of Section 251 of the Telecommunications Act. Verizon v. FCC, 535 U.S. 467, 503-505; 122 S. Ct. 1646, 1668; 152 L.Ed. 2d 701, 732-33 (2002). Accordingly, SBC's rates for UNEs must comply in all respects with the TELRIC rules. Staff IB at 21-22.

2. ICC TELRIC Proceedings

The Commission has successfully applied TELRIC principles in prior dockets. First, in its *Second Interim Order*, Investigation into forward looking cost studies and rates of Ameritech Illinois for interconnection, network elements, transport and termination of traffic, ICC Docket Nos. 96-0486 / 96-0569 (consol.) (February 17, 1998)(hereafter "TELRIC Order"), the Commission set TELRIC rates for SBC. *See, generally*, TELRIC Order. In its TELRIC Order, the Commission established a cost of capital, depreciation, fill factors, and shared and common cost load to be used by SBC in establishing TELRIC-compliant UNE rates, and directed SBC to re-run its cost studies using those inputs. TELRIC Order at 21, 26-7, 32-4, 46-53, 138. The Commission further found that

SBC had failed to support its non-recurring charges, and, indeed, had filed tariffs that "ma[de] it impossible for the Commission, new entrants and even [SBC] itself, to cogently determine how and when nonrecurring charges apply." TELRIC Order at 91-93. The Commission, accordingly, directed the use of interim non-recurring rates until such time as SBC filed a conforming tariff. Id. at 138.

SBC filed tariffs and cost studies purporting to support the non-recurring charges the Commission disallowed in the *TELRIC Order*. See *Order* at 1-3, Illinois Commerce Commission On Its Own Motion: Investigation into the compliance of Illinois Bell Telephone Company with the order in Docket 96-0486/0569 Consolidated regarding the filing of tariffs and the accompanying cost studies for interconnection, unbundled network elements and local transport and termination and regarding end to end bundling issues, ICC Docket No. 98-0396 (October 16, 2001) (hereafter "TELRIC II Order"). The Commission found SBC's tariffs and cost studies to be satisfactory in some respects and with respect to some NRCs, but not to others. *See, generally*, TELRIC II Order. The Commission reopened the TELRIC II proceeding, and adopted interim NRCs, some of which remain in effect. *See, generally*, *Order on Reopening*, Investigation into the compliance of Illinois Bell Telephone Company with the order in Docket 96-0486/0569 Consolidated regarding the filing of tariffs and the accompanying cost studies for interconnection, unbundled network elements and local transport and termination and regarding end to end bundling issues, ICC Docket No. 98-0396 (April 30, 2002) (hereafter "TELRIC II Order on Reopening"). Finally, the Commission set rates for SBC's unbundled local switching UNE. *See, generally*, *Order,* Illinois Commerce Commission On Its Own Motion v. Illinois Bell Telephone Company: investigation into Tariff Proceeding Providing unbundled Local Switching with Shared Transport, ICC Docket No. 00-0700 (July 12, 2002) (hereafter "TELRIC 2000 Order"). Accordingly, it can be fairly said that the Commission has ample experience in TELRIC proceedings.

3. Burden of Proof

SBC bears the burden of proof in this proceeding. Staff IB at 27.

A. Economic/Policy Issues Associated With UNE Pricing (Including Benchmarking Analyses and Trends in Telecommunications Cost)

The economics of UNE pricing is clearly an issue at the heart of this proceeding. Staff IB at 29 *et seq*.; see also, generally, Staff Ex. 2.0; Staff Ex. 22.0. SBC argues that what it perceives to be artificially low, allegedly non-compensatory UNE prices do considerable harm to the telecommunications industry, stifling investment by CLECs in telecommunications facilities, causing them to rely on ILECs, giving them incentives to serve only the most profitable customers, and causing other perceived undesirable economic outcomes. *See, e.g.*, SBC Ex. 2.0 at 33-39. The CLECs counter this argument by arguing that it is largely irrelevant, since UNE prices are not, in fact, artificially low, and that SBC's attempts in this proceeding to demonstrate that UNE rates are artificially low and non-compensatory are unconvincing and defective. Joint CLEC Ex. 2.0 at 23 *et seq*.

The Staff recommends that the Commission not attempt to encourage competition through artificially low UNE prices, which are prices lower than forward looking costs for an efficient firm. Staff IB at Staff Ex. 2.0; Staff Ex. 22.0. This type of social engineering will have many of the negative implications ascribed to it by SBC. Id. On the other hand, the Staff recommends that the Commission not *discourage* competition by allowing SBC to charge excessively *high* UNE rates, which are rates *higher* than forward looking costs for an efficient firm. Id. There are a number of reasons for this. Permitting SBC to overcharge for UNEs will lead to: (1) excess profits for SBC Illinois; (2) higher prices for consumers; (3) inefficient and unnecessary duplication of facilities; (4) reduced competition; and (5) less consumer choice. Id.

In summary, the Staff urges the Commission to set UNE-L rates precisely as it has done in the past: by determining SBC's forward-looking costs for providing UNE-L in a manner consistent with forward looking costing principles. Staff IB at 34.

4. Recurring Rates Inputs

a) Fill Factors

Staff observes that SBCI's LoopCAT model uses SBCI's actual fills to develop forward-looking loop costs. *See, generally*, Staff IB at 37, et seq., Staff Ex. 17.0 at 19. In light of this, Staff contends that SBCI's use of its actual fills is not compliant with TELRIC principles because it does not represent the forward-looking fills of an efficient carrier. Staff Ex. 17.0 at 30-31; see also Staff Ex. 10.0 at 4-15, 16-18; Staff Ex. 32.0 at 1-11; Staff Ex. 2.0 at 14-22; Staff Ex. 22.0 at 9-

17, 30, 39-40; Staff Ex. 25.0 at 1-34. On the other hand, Staff asserts that various CLECs' proposals to use usable capacity fill or target fill also fail to capture the level of fill (or conversely, spare capacity) that an efficient carrier would include in a network today. Staff IB at 46, et seq., Staff Ex. 17.0 at 19, et seq. Staff avers that the ideal information upon which to base the forward-looking fills of an efficient carrier is not readily available, and therefore proposes that the Commission require use of adjusted actual fill factors. Staff IB at 55, et seq., Staff Ex. 17.0 at 35, et seq. Staff contends that its approach recognizes that SBCI's actual fills are an appropriate *starting point* from which to determine efficient forward looking fills, yet avoids overestimating the efficiencies that could be achieved by a forwarding looking, efficient carrier. Id.; see also Staff Ex. 25.0 at 10, et seq.

b) Depreciation

Staff asserts that the Commission should adopt the forward-looking equipment lives developed by the FCC and ordered by this Commission in its *TELRIC Order*. Staff IB at 64, et seq.; Staff Ex. 13.0 at 3. Staff claims that the use of these lives is competitively neutral, encourages efficient competition and fairly balances the interests of ratepayers with subscribers. Staff IB at 64, et seq.; Staff Ex. 2.0 at 24, et seq; Staff Ex. 15.0 at 3, et seq.; Staff Ex. 22.0 at 24, et seq. In contrast, the Staff contends that financial reporting lives as proposed by SBCI unduly protect the interest of shareholders at the expense of wholesale and ultimately retail subscribers who will be required to pay higher rates in order to eliminate any possible obsolescence risks to shareholders. Id.

c) Cost of Capital

Staff proposes an overall cost of capital of 8.62%. See, generally, Staff IB at 69, et seq.; Staff Ex. 12.0, Schedule 12.1; *see also* Staff Ex. 31.0, 36.0. Staff proposes capital structure of 4.78% short-term debt, 44.22% long-term debt, and 51.00% common equity. Id. Staff further recommends a 12.44% cost of common equity; a 4.99% cost of long-term debt; and a 1.47% cost of short-term debt. Id.

Staff's proposal is far preferable to the alternatives presented by other parties. First, Staff presents a capital structure that reasonably balances debt and equity, and accurately reflects the capital structure of other industrial enterprises having reasonable levels of financial strength. Id. SBCI, in contrast, proposes an unnecessarily expensive capital structure with a level of equity far in excess of that necessary to maintain a reasonable level of financial strength. Id. Further, Staff's recommendation reflects a level of competitive risk that is consistent with the degree of efficiency reflected in the other cost components of Staff's proposed UNE loop rates. Id. Likewise, Staff's recommended cost of debt takes into account recent downward trends in interest rates, instead of speculating that interest rates will increase to levels experienced in 1999. Id.

d) Cable Installation and DLC Engineering, Furnishing and Installation ("EFI") Factors

Staff notes that SBCI develops Cable Installation and DLC Engineering, Furnishing and Installation ("EFI") Factors for use in its LoopCAT model to determine UNE loop costs that are then input into specific costs studies, which are used in calculating total direct loop costs under TELRIC. Staff IB at 104 et seq.; Staff Ex. 3.0 at 17, et seq. Staff states that it has identified deficiencies with SBCI's development of these factors, specifically, that the company did not demonstrate that the costs developed represent the forward-looking costs of an efficient carrier, and that actual data used was old, historical data. Id.; see also Staff Ex. 3.0 at 18-20. Staff considers the key points of its analysis to be that the company makes no effort to isolate the costs of new network construction (whether in new developments or in existing neighborhoods), and fails to capture costs that reflect the economies of scale that would be realized from complete (rather than piecemeal) construction of a new network. Id. As a result, Staff is of the opinion that the historical data relied on by SBCI unquestionably overestimates costs. Id. Staff observes that a number of its recommended changes to these factors were accepted by SBCI and included in subsequent LoopCAT processes, thereby reducing the costs somewhat. Staff IB at 105-106; Staff Ex. 3.0 at 20, et seq.; Staff Ex. 23.0 at 2, et seq. However, Staff avers that these revisions did not correct all of the deficiencies that it identified. Therefore, Staff recommends that the company update the data as suggested by Staff, to reflect forward-looking costs of an efficient carrier, and that costs studies be revised to reflect those changes. Staff IB at 107 et seq; Staff Ex. 23.0 at 2-11.

e) Fiber/Copper Crossover Point

Staff observes that LoopCAT employs a 12,000-foot crossover point, which identifies the maximum loop length (as measured from the central office to the distribution terminal) for which both the feeder and distribution portion of the loop will utilize copper cable. Staff IB at 110 et seq., Staff Ex. 4.0, generally. Staff further observes that, for loops exceeding the crossover point, LoopCAT costs a loop based on utilization of fiber feeder cable, Next Generation Digital Loop Carrier ("NGDLC") equipment, and copper distribution cable. Staff Ex. 4.0 at 10-24. Staff Ex. 24 at 9-14 Staff contends that SBCI's utilization of a 12,000-foot crossover point is inefficient and unnecessarily inflates costs, because it designs a network that includes too many NGDLCs. Id. Staff recommends that loop costs be determined on the basis of an 18,000-foot crossover point. Staff Ex. 4.0 at 19.

f) Other DLC Investment Cost Issues

Staff states that, in addition to designing a network that includes too many NGDLCs, the LoopCAT model exacerbates this problem by allowing for a very limited number of Remote Terminal ("RT") cabinet sizes to house the NGDLCs – which results in an even more inefficient network design that unnecessarily inflates per loop costs. Staff IB at 118 et seq.; Staff Ex. 4.0 at 14-15. Staff observes that, although there are ten sizes of RT cabinets available form SBCI's vendor, SBCI's original LoopCAT model only included the two largest cabinet sizes. Id. Because the larger size cabinets cost more than the smaller size cabinets, Staff contends that LoopCAT's incorporation of what is essentially a "one size fits all" network design is likely to needlessly inflate per loop costs, since LoopCAT automatically incorporates the higher costs of a large cabinet even if a smaller and less expensive cabinet would meet applicable capacity requirements. Id.; see also Staff Ex. 24.0 at 4-6. Staff notes that SBCI's rebuttal filing and revised LoopCAT study make clear that LoopCAT can be modified to include additional RT cabinet sizes. Staff Ex. 24.0 at 7-8. It is also clear, avers the Staff, that substantial cost reductions can be obtained by adding two additional RT equipment choices. Id. Therefore, Staff recommends that the Commission require SBCI to produce LoopCAT runs for all of its loop types in all access areas to determine the impact of including each of the RT cabinet types currently excluded, and to use the least cost mix of RT cabinets in its final loop cost development. Id.; see also Staff IB at 121-22.

g) Premises Termination Costs

Staff states that its adjustment to SBCI's premises termination costs results from a proposed adjustment to the company's labor time estimates for NID and drop wire installation costs, and Staff's proposed modifications to SBCI's capital cost factor which flow into the calculation of labor rates. Staff IB at 125, et seq.; Staff Ex. 5.0 at 32-33. However, Staff contends that distribution terminal costs are no longer at issue because SBCI removed distribution terminal investment costs from LoopCAT after discovering those costs were being aggregated in cable accounts and therefore being double counted. Staff Ex. 22.0 at 31, 41-42. One of Staff's concerns regarding premises termination costs was the SME estimate for travel time incorporated into each labor estimate. Staff IB at 126, et seq.; Staff Ex. 3.0 at 30-33; Staff Ex. 23 .0 at 12-16. Staff developed revised travel time estimates based on one roundtrip between the company's facilities and an installation area, with shorter travel times from one end user's premises to the next. Id. Staff recommends that these revised installation time estimates be used to develop premises termination costs. Id.

5. Nonrecurring Rate Issues

Staff observes that non-recurring charges (hereafter "NRCs") are one-time charges that a CLEC incurs for use of an ILEC's network. Staff IB at 134 et seq.; Staff Ex. 6.0 at 4, et seq. CLECs may use that network for end users migrating their existing service to a CLEC or establishing a new service with a CLEC. Id. Examples of NRCs are service order changes, loop connection services, and services associated with connecting to the switch. Id. NRCs are also incurred in connection with certain changes to an end user's service, such as when adding "Caller ID" or some other central office feature to an existing account. Id.

Staff contends that, in developing its NRC cost estimates, SBC did not give the subject matter experts it relied on a free hand in supplying inputs, but rather confined them to describing existing or anticipated SBC processes and technology. Staff IB at 139, et seq.; Staff Ex. 7.0, generally. Furthermore, Staff asserts that these subject matter experts were not presented as witnesses in this proceeding, and the record in this proceeding contains little information regarding the identities of these people, much less what they might say regarding the performance of the tasks they were assigned by SBC. Id.; see also SBC Ex. 5.0, 5.1, 6.0; Tr. at 1139-1141,1147-48, 1412, 1448, 1458-59. Staff states that these facts, in conjunction with the failures of the witnesses SBC did supply, show that the Commission cannot be confident that the nonrecurring rates it adopts in this proceeding will be sufficiently supported as to constitute permanent rates. Staff IB at 145-47.

While the information presented by SBC in this proceeding does not, in Staff's view, support the adoption of permanent nonrecurring provisioning costs and resulting rates, Staff notes that the Commission is certainly presented with much more extensive and complete information in this proceeding than it was presented with when determining many of its existing nonrecurring rates, many of which are, in fact, the product of inter-party negotiations. Id. For these reasons, Staff recommends the Commission adopt as interim rates subject to true-up SBC's proposed rates with the adjustments proposed by Staff below and with any intervenor proposed adjustments the Commission finds appropriate. Id.

a) Service Order NRC Studies

Staff contends that SBC's proposed non-recurring service ordering charges are inflated due to an overly pessimistic calculation of electronic flow through rate for service orders. Staff IB at 148, et seq.; Staff Ex. 11.0, generally. Except for EELs, SBC's proposed non-recurring service ordering charges are, Staff contends, based simply on historical levels of service order flow through, contrary to the FCC's definition of TELRIC. Staff IB at 151; Staff Ex. 11.0 at 9, et seq. Staff asserts that, by basing electronic flow through rates on the <u>actual</u> levels attained in July, August, and September, 2002, SBC has understated the appropriate levels of flow through for TELRIC purposes, thereby overly inflating service ordering charges. Id. The Staff recommends that the Commission adopt the same flow through rates it adopted in its TELRIC II Order, where it ordered a 98% flow through rate be used to determine non-recurring service order costs. Staff IB at 155-56; Staff Ex. 11.0 at 20-21.

b) Provisioning NRC Studies

Staff points to SBC's claims that the Special Services Center (SSC) / Local Operations Center (LOC) and Circuit Provisioning Center (CPC) / Hi-Cap Provisioning Center (HPC) conduct numerous and expensive testing activities when provisioning loops. See, generally, SBC Ex. 6.0. Staff asserts that SBC has provided virtually no support, and certainly no credible support, for the charges associated with these activities. Staff IB at 156 et seq.; see also Staff Ex. 7.0, generally. Staff states that, when it identified discrepancies in SBC's studies, SBC not only failed to provide support for its initial estimates, but also made changes to its studies and failed *again* to support these changes. Id. Staff considers it possible that some testing by SSS/LOC and CPC/HPC is consistent with TELRIC. Id. However, Staff contends that SBC has utterly failed to prove this to be the case. Id. In the absence of credible evidence to support the work performed by these groups in provisioning UNE loops, Staff recommends that the Commission not permit SBC to assess charges for either standalone loops or for EEL loops, which include costs related to the SSC/LOC and CPC/HPC groups. Id.

Staff notes that, in presenting its NRC loop provisioning cost estimates, SBC's evidence shows that its CP&M group can provision cross connects on the customers' side of UNE loops in less time than its DOG group. Staff IB at 161;

Staff Ex. 7.0 at 38-39, 50; Staff Ex. 27.0 at 17-18, 28. Moreover, Staff notes that SBC has offered no technological reason for the existence of this difference; instead, it has argued that CP&M does the job more quickly due to the way CP&M is structured. Id. Thus, opines Staff, SBC has done nothing more than demonstrate that its DOG group is inefficient when provisioning UNE loops. Id. To remedy this problem, Staff recommends that the Commission order SBC to replace the its EEL loop DOG provisioning estimates with the CP&M provisioning costs SBC estimates for stand alone loops. Id.

Staff observes that SBC, in presenting its EEL dedicated transport and multiplexing provisioning cost estimates, has failed to explain why every task performed when multiplexing is established in conjunction with an order for dedicated transport needs to be performed *again* when a separate multiplexing order is placed. Staff IB at 162, et seq.; Staff Ex. 7.0 at 49-50; Staff Ex. 27.0 at 28. Staff notes that SBC nonetheless assumes that *every* task *always* has to be performed twice, or at least *charged for* twice, even if, as appears likely, it is only done once. Id. In particular, Staff contends that SBC does not explain whether requesting CLECs are charged for multiplexing twice because they are required by SBC's ordering systems to place two separate orders when initially establishing an EEL. Id. Staff further asserts that SBC does not explain whether it must repeat every task required to initially provision multiplexing when a CLEC requests a reconfiguration of the multiplexing arrangement in future periods. Id. To ensure that SBC does not assess charges twice for work activities that it performs once, Staff recommends that the Commission order SBC to refrain from assessing multiplexing charges in combination with orders for dedicated transport. Id. Instead, Staff asserts that the Commission should permit SBC to assess these charges if and only if CLECs request reconfiguration of existing multiplexing arrangements. Staff IB at 164.

Staff argues that SBC has failed to provide information that would ensure that this change alone would eliminate any chance of double counting for multiplexing work. Staff IB at 164. By way of example, Staff notes that it is unclear whether every activity that SBC performs to initially configure multiplexing needs to be repeated when reconfiguring multiplexing. Id. This change, however, would certainly eliminate double counting of activities for initial installations. Id.

Staff points out that, based on SBC's application of its DOP factor to UNE-P provisioning, the company has misapplied its DOP factor to Standalone UNE POTS Loop provisioning. Staff IB at 165, et seq. Staff Ex. 7.0 at 61. Staff recommends that the Commission reject the CP&M work group occurrence factor of ***BEGIN CONF 36.60% END CONF*** presented by SBC. Id. Instead, the Staff recommends that the Commission require SBC to assume a CP&M work group occurrence factor for standalone POTS UNE loops equal to ***BEGIN CONF 3.99% END CONF*** or, in the event a different DOP factor is adopted in this proceeding, ***BEGIN CONF 10.9% END CONF*** times (1 – the DOP factor adopted in this proceeding). Staff IB at 170; Staff Ex. 27.0 at 33, n. 63. This proposed rate, opines Staff, corrects the inconsistency in SBC's cost studies by assuming that CP&M work group occurrence factor are the same for

Standalone UNE POTS loops as they are for UNE-P POTS loops. Staff Ex. 7.0 at 62-63.

Staff observes that, in developing its UNE-P POTS Loop Line Connection Cost estimates, SBC assumes that its Field Operations Group (FOG) provisioning group will need to install cross connects and perform related activities in the central office a certain percentage of time; the work group occurrence factor is equal to that figure. Staff IB at 171, et seq.; see also Staff 7.0 at 63, et seq. Staff notes that SBC assumes the same FOG work group occurrence factors in removal of cross connects and related activities in the central office. Id. Staff asserts that SBC failed to account for instances where a customer served by a CLEC UNE-P migrates back to SBC retail service or to a CLEC providing service using the loop and switching elements. Id. Staff contends that SBC's study assumes that customers served via UNE-P never migrate to another provider (including SBC), which uses SBC facilities. Id. SBC has, in Staff's view, failed to address this concern. *See* Staff Ex. 27.0 at 37 Therefore, Staff recommends that the Commission reject SBC's proposed FOG work group occurrence factors with respect to removal of cross connects and related activities in the central office. Staff IB at 172.

Staff points to the fact that SBC proposes to include both installation and disconnection in the estimates of UNE connection costs and to use a 2-year location life for purposes of discounting disconnection costs. Staff IB at 173, et seq.; Staff Ex. 7.0 at 40, 46-47, 60, 63, 67. Staff contends that SBC has failed provide credible support for its 2 year location life assumption or provide credibly supported revised location life estimates. Id. Staff therefore recommends that the Commission direct SBC to calculate the location life for each loop type based upon the average location life of SBC's comparable end-user offerings. Staff IB at 178-79; Staff Ex. 6.0 at 32. Staff recommends that the Commission adopt a 4-year location life for the purpose of discount disconnection charges. Id. Regardless of which location life the Commission directs SBC to adopt, Staff recommends that it nonetheless direct SBC to begin assessing separate connection and disconnection fees when its billing systems are able to do so in the first quarter of 2005. Staff IB. at 179; Staff Ex. 27.0 at 39, 42.

Staff indicates that SBC states in its initial filing that its physical provisioning groups performed activities to convert special access circuits to UNE combinations. Staff IB at 180, et seq.; see also Staff Ex. 7.0 at 27, 30-31; Staff Ex. 27.0 at 7. Staff observes that SBC listed in support of two charges for special access to UNE conversions, the following activities: the Design & Coordination charge and the Demarcation Retag charge. Id. Further, Staff notes that SBC thereafter withdrew its proposal to assess a Demarcation Retag charge. Id. SBC's testimony provides, according to Staff, strong evidence that its Design & Coordination charge, which it continues to support, is grossly inflated at best and perhaps entirely inappropriate. Id. Staff moreover contends that SBC has been unable to respond to further attempts to discern what, if any, activities its provisioning groups would need to perform in a forward looking environment in order to actually convert special access circuits to UNE combinations. Staff IB at 185.

c) Switch Port And Features NRC Studies

Staff did not address this issue in its testimony in this proceeding, but reserved the right to respond to any arguments raised in the parties' initial briefs.

d) Labor Rates

Staff contends that SBC did not develop the NRCs it proposes in this proceeding in a manner consistent with TELRIC ratemaking principles. Staff IB at 185, et seq.; Staff Ex. 6.0 at 11. In particular, Staff asserts that SBC's use of the so-called "support asset factor" ("SAF"), as an adder to wage rates is directly contrary to TELRIC principles, and to prior Commission orders. Id.; Staff Ex. 6.0 at 16. Staff notes that the "support assets factor" assigns costs of certain physical assets directly to the labor rates of employees who use those assets. Id. at 11. Accordingly, Staff notes, the use of the SAF adds significantly to the labor rate of certain classes of employees. Id. In short, the addition of the SAF increases the level of labor rates. Id. Since labor costs are a major component – perhaps, the major component -- of total costs in the determination of non-recurring network element costs, Staff observes that this change in method significantly, and improperly, increases NRCs. Id. Staff recommends that the SAF be eliminated from labor rates, and if applicable, the costs in the SAF be included as part of the company's common costs that are allocated to both retail and wholesale services. Staff IB at 188-89.

6. Shared And Common Cost Factors

SBC claims that its Shared and Common ("S&C") factor is the most accurate representation of its shared and common costs. Staff IB, at 189. Staff, however, disagrees with SBCI's methodology for recovering shared and common costs. Staff identified several fundamental flaws in SBCI's proposal for shared and common cost recovery, and proposes changes to the methodology to correct those flaws. *Id*. For instance, the SBCI proposed shared cost denominator (the Common Costs denominator multiplied by the Wholesale Direct Cost Percentage) is grossly understated when compared with the extended TELRIC for UNE services and wholesale services. Staff RB, at 90-91. Further, if SBCI can prove -- which up to this point it has not -- that there actually are shared wholesale costs (UNE + other wholesale), then it must develop a denominator that includes all UNE direct costs *plus* all other wholesale direct costs. *Id*. On the other hand, if SBCI cannot prove it has shared wholesale costs, Staff recommends that the appropriate formula be as follows:

> (zero/any number + total common costs/total direct costs) * (1 + uncollectible %) = S&C markup[1]

However, if SBCI can prove that it has "shared wholesale costs," then Staff recommends that SBCI develop a "wholesale shared denominator" that includes both UNE direct costs based on extended TELRIC *plus* all other wholesale direct costs. *Id*. Unless both UNE direct costs and other wholesale direct costs are

---

[1] If the Commission accepts Staff's recommendation that SBCI has failed to provide any evidence supporting their proposed shared wholesale costs, it should also: (1) move the SBCI proposed Wholesale Marketing Costs from shared costs to common costs, and (2) make the Account 67XX adjustments as proposed by SBCI (SBC Ill. Ex. 7.2 (Barch), Sched. DJB-S01). Both of which would reduce Staff's proposed Shared & Common Cost Factor from 10.65% to 10.22%, with an uncollectible factor of 3.93%.

included in the denominator, then the numerator and denominator will be mismatched and will not provide a reasonable or reliable ratio of shared costs to be applied to UNEs. *Id*. Staff recommends that the Commission expressly find that the SBCI proposed methodology is inappropriate and specifically reject it. *Id*. Staff also recommends that the Commission accept SBCI's offer to implement Staff's proposed methodology for the shared cost denominator and order SBCI to develop the shared cost denominator methodology advocated by Staff, a number that includes both UNE direct costs based on extended TELRIC plus all other wholesale direct costs.

7. Annual Charge and Other Factors

The Staff notes that Annual Charge Factors ("ACFs") are factors that are applied to the total investment for a piece of network equipment to derive the total annual cost of providing the equipment. Staff IB at 217, et seq.; Staff Ex. 4.0 at 24-29. Except for SBCI's automatic adjustment of maintenance expense as fill factors increase, Staff did not take issue with the methodology employed by the company to calculate ACFs. Id. Staff however, asserts that a number of inputs used in SBCI's ACF Study are improper. Id. Specifically, Staff contends that the Commission should reject the sales tax rate, the cost of capital, cost of debt and debt-to-equity ratio and average service lives and salvage values that SBCI proposes. Id.

One aspect of SBCI's ACF Study methodology that Staff urges the Commission to reject is the automatic adjustment of maintenance expense as fill factors increase. Staff IB at 218; Staff Ex. 2.0 at 24, 26-27; see also Staff Ex. 10.0 at 16-18. Staff asserts that, as a result of Staff's fill factor adjustments, there is no credible basis to conclude that changes need to be made to ACFs, and accordingly this improper aspect of SBCI's ACF Study was avoided in calculating Staff's revised ACFs. Id. Staff recommends that its proposed ACFs as set forth in Staff Ex. 24.0, Schedule 24.04P be utilized in setting SBCI's UNE loop rates. Staff Ex. 4.0, Schedule 4.01P; Staff Ex. 24.0 at 28-29, Schedule 24.04P.

Imputation

Staff contends that any increase to UNE loop rates resulting from this proceeding would require that SBC's retail business network access lines satisfy a so-called imputation test, as established by the General Assembly in Section 13-505.1 of the Public Utilities Act, and the Commission's administrative rules promulgated under the authority of the statute. Staff IB at 220; see als0 220 ILCS 5/13-505.1; 83 Ill. Admin. Code §792.10, et seq. Staff argues that SBC's UNE-L offering is a "noncompetitive service or noncompetitive service element" within the meaning of Section 13-505.1(a), and its business network access line rates, which are competitive services, must therefore satisfy imputation Staff IB at 220-225. Staff contends that SBC's so-called "price squeeze" analysis, and the Joint CLECs' imputation test, are defective and do not comply with either the letter or spirit of the imputation statute. Staff IB at 228, et seq. Accordingly, the Staff recommends that its imputation methodology and test be adopted. Staff IB at 230, et seq.; see also Staff Exhibit 24.0, Schedule 24.01; Staff Ex. 33.0 at 13-14; Schedule 33.01. Were SBC's proposed UNE-L rates to be adopted, it would, under Staff's test, be required to raise its business NAL rates significantly. Staff IB at 231.

8. Recommended Rates

Staff recommends that the Commission adopt the Staff adjustments recommended above which are reflected in the rates presented by Staff in the table below, under the heading "Staff UNE Rate". If the Commission does not accept Staff's recommendation, and determines that input changes recommended by Staff and other parties should be used to develop UNE loop and NRC rates, Staff recommends that the Commission provide those changed input amounts in its order in this proceeding and have both SBCI and Staff rerun the LoopCAT model and the various costs studies necessary to develop TELRIC costs, then apply the Commission-approved Shared and Common cost allocator to those costs to determine new UNE loop and NRC rates in Illinois. If the Commission is undecided on NRC costs, Staff recommends as an alternative that the Commission order that Staff's proposed NRC adjustments, which are reflected in the rates set forth in Schedules 26.1 through 26.5 be ordered made along with any appropriate intervenor adjustments until such time as the company can file new NRC rates based on costs for which it has provided acceptable proof.

COMPARISON OF CURRENT, STAFF AND SBCI RECURRING UNE RATES

Loop Type	Zone	Current UNE Rate	Staff UNE Rate	Staff % Change to Current Rate	SBCI UNE Rate	SBCI % Change to Current Rate
2 Wire Analog Loop	A	$2.59	$4.97	92.0%	$9.03	248.6%
	B	$7.07	$8.62	21.9%	$17.82	152.1%
	C	$11.40	$10.94	-4.2%	$20.56	80.4%
Ground Start Loop	A	$2.64	$4.01	51.9%	$7.56	186.3%
	B	$7.84	$8.02	2.2%	$18.81	139.9%
	C	$12.38	$11.62	-6.6%	$23.05	86.2%
COIN Loop	A	$2.67	$4.01	50.2%	$7.57	183.4%
	B	$8.09	$8.04	-0.6%	$19.02	135.1%
	C	$12.72	$11.75	-8.3%	$23.37	83.7%
EKL Loop	A	$2.95	$4.01	36.0%	$7.73	162.2%
	B	$12.18	$8.60	-41.6%	$23.16	90.1%
	C	$17.92	$14.31	-25.3%	$29.78	66.2%
4 Wire Analog Loop	A	$4.08	$8.02	96.6%	$15.17	271.9%
	B	$16.82	$16.22	-3.7%	$39.01	131.9%
	C	$26.63	$24.08	-10.6%	$48.26	81.2%
BRI (ISDN) Loop	A	$2.71	$4.97	83.6%	$9.48	249.9%
	B	$8.88	$9.69	9.1%	$26.48	198.2%
	C	$13.68	$15.18	11.0%	$32.31	136.2%
DS1 Loop	A	$73.46	$25.17	-191.9%	$39.00	104.9%
	B	$61.45	$38.63	-59.1%	$61.33	101.0%
	C	$61.45	$50.58	-21.5%	$84.48	37.5%
2W xDSL Compatible Loop	A	$2.59	$4.97	92.0%	$8.91	244.1%
	B	$7.07	$8.63	22.1%	$16.13	128.2%
	C	$11.40	$12.56	10.2%	$23.18	103.3%
4W xDSL Compatible Loop	A	$4.08	$8.02	96.6%	$14.68	259.8%
	B	$16.82	$15.39	-9.3%	$29.24	73.9%
	C	$26.63	$23.40	-13.8%	$43.62	63.8%
DS3 Digital Loop	A		$282.18		$413.19	
	B		$341.65		$504.11	
	C		$445.87		$664.64	

WHEREFORE, for all the reasons set forth herein, the Staff of the Illinois Commerce Commission respectfully requests that its recommendations be adopted in this proceeding.

Respectfully submitted,

Carmen L. Fosco
Matthew L. Harvey
Michael J. Lannon
Office of General Counsel
Illinois Commerce Commission
160 North LaSalle Street
Suite C-800
Chicago, Illinois 60601
(312) 793-2877

Counsel for the Staff of the Illinois Commerce Commission

April 19, 2004